Avoiding Possible U.S. Protectionism: The Benefits of Secure Market Access

In the medium-term economic projections released as part of the White Paper on Tax Reform, the government projected that real GDP would grow on average about 3 per cent a year over the next five years. Consistent with this projection, employment was expected to rise an average of 2.2 per cent, or about 260,000 jobs per year. The White Paper recognized that the risks facing the achievement of this economic performance were substantial: "...failure of the U.S. government to achieve substantial deficit reduction, weak domestic demand growth in overseas countries and lack of progress in re-balancing trade flows among the largest industrialized countries could well set the stage for an environment in which the U.S. dollar falls sharply, U.S. protectionism increases, international interest rates rise, and the risks of financial disruption arising from the international debt burdens of the developing countries increase".[12]

The Department of Finance analysis and estimates of the macroeconomic impacts of the Canada-U.S. Free Trade Agreement presented in Chapter IV and the preceding section of this chapter assumed a continuation of the current international trading environment. By so doing, they likely understate the economic benefits flowing from the Agreement, particularly through its provision of more secure access to U.S. markets. In the absence of the Agreement, the possibility of growing U.S. protectionism places the status quo trading environment at considerable risk. Thus, the positive economic benefits from the Agreement are likely larger than those estimated by examining only the impacts of the elimination of existing trade barriers.

To illustrate the potential gains from the Agreement as a result of increased security of access to the U.S. market, the Department of Finance's macroeconomic model of the Canadian economy was used to estimate the impacts on the Canadian economy over the 1989 to 1993 period of a scenario in which trade relations between the two countries deteriorated in the absence of a trade agreement. Clearly, it is difficult to be precise as to how much additional protectionist measures might be imposed by the U.S. in the absence of the Agreement, and as to Canada's possible responses. For this analysis, the illustrative scenario assumed additional protection imposed by the U.S. equivalent to a 5-percentage-point increase in U.S. tariffs. It also assumed that Canadian tariffs vis-à-vis the United States were increased proportionally in response.

Significant increases in U.S. protectionism would have a pervasive negative effect on the Canadian economy. The initial impact would be in export-based industries, with reduced Canadian production, investment and employment. But the negative effect would be wider, as the impact of higher tariffs on prices reduced household purchasing power. As the real incomes of Canadians fell, their demands for domestic Canadian products would also decline, spreading the negative impacts on income,

[12] The Honourable Michael H. Wilson, Department of Finance, Tax Reform 1987, *Economic and Fiscal Outlook*, Minister of Supply and Services Canada, Ottawa: June 18, 1987, p. 23.